(iii) For the definition of ''educational institution'', see §1.151–3(c).

(4) *Illustrations.* The application of this paragraph may be illustrated by the following examples:

Example 1. During the 1982 taxable year, A, a married taxpayer, incurs and pays employment-related expenses of $4,000 for the care of a qualifying individual. A's earned income for the taxable year is $20,000 and his wife's earned income is $1,500. Under these circumstances, the amount of employment-related expenses for the year which may be taken into account under §1.44A–1(a) is $1,500, determined as follows:

Employment-related expenses incurred during taxable year ($4,000, but limited to $2,400 by paragraph (a)(1) of this section), ... $2,400

Application of paragraph (b)(1)(ii) of this section (employment-related expenses, may not exceed wife's earned income of $1,500 . . . . . $1,500

Employment-related expenses taken into account $1,500

Example 2. Assume the same facts as in *Example 1* except that A's wife is a full-time student for nine months of the taxable year and earns no income for the year. Under these circumstances, the amount of employment-related expenses for the year which may be taken into account under §1.44A–1(a) is $1,800, determined as follows:

Employment-related expenses incurred during taxable year ($4,000, but limited to $2,400 by paragraph (a)(1) of this section $2,400

Application of paragraph (b)(3) of this section [employment-related expenses may not exceed wife's earned income of $1,800 (200×9) . . $1,800

Employment-related expenses taken into account $1,800

(Secs. 44A(g) and 7805 of the Internal Revenue Code of 1954 (90 Stat. 1565, 26 U.S.C. 44A(g); 68A Stat. 917, 26 U.S.C. 7805))

[T.D. 7643, 44 FR 50334, Aug. 28, 1979, as amended by T.D. 7951, 49 FR 18092, Apr. 27, 1984]

§1.44A–3 Special rules applicable to married individuals.

(a) *Joint return requirement.* This section applies only if the taxpayer is married at the close of a taxable year in which employment-related expenses are paid. In such a case the credit provided by section 44A with respect to employment-related expenses is allowed only if for the taxable year the taxpayer and his or her spouse file a joint return. If either spouse dies during the taxable year and a joint return may be made for the year under section 6013(a)(2) for the survivor and the deceased spouse, the credit is allowed for the year only if a joint return is made. If, however, the surviving spouse remarries before the end of the taxable year in which his or her first spouse dies, a credit is allowed on the separate return which is made for the decedent spouse. For purposes of this section, certain married individuals legally separated or living apart are treated as not married, as provided in paragraphs (b) and (c), respectively, of this section.

(b) *Marital status.* For purposes of section 44A, an individual legally separated from his or her spouse under a decree of divorce or of separate maintenance is not considered as married.

(c) *Certain married individuals living apart.* For purposes of section 44A, an individual who is married within the meaning of section 143(a) is treated as not married for the entire taxable year, if the individual—

(1) Files a separate return for the year,

(2) Maintains as his or her home a household which constitutes for more than one-half of the taxable year the principal place of abode of a qualifying individual, and

(3) Furnishes over one-half of the cost of maintaining the household for the year,

and if the individual's spouse is not a member of the household at any time during the last 6 months of the year. Thus for example, an individual who is married during the taxable year, but is treated as not married by reason of this paragraph, may determine the earned income limitation upon the amount of employment-related expenses without taking into account the earned income of his or her spouse under §1.44A–2(b).

[T.D. 7643, 44 FR 50335, Aug. 28, 1979]

§1.44A–4 Other special rules relating to employment-related expenses.

(a) *Payments to related individuals*—(1) *Taxable years beginning after December 31, 1978.* For taxable years beginning after December 31, 1978, a credit is not allowed under section 44A with respect to the amount of any employment-related expenses paid by the taxpayer to an individual—

(i) With respect to whom for the taxable year a deduction under section 151(e) (relating to deduction for personal exemptions for dependents) is allowable either to the taxpayer or his or her spouse, or

(ii) Who is a child of the taxpayer (within the meaning of section 151(e)(3)) who is under age 19 at the close of the taxable year.

For purposes of this paragraph (a)(1), the term ''taxable year''means the taxable year of the taxpayer in which the service is performed. (1943)

(2) *Taxable years beginning before January 1, 1979.* For taxable years beginning before January 1, 1979, except as otherwise provided in paragraph (a)(3) of this section, a credit is not allowed under section 44A with respect to the amount of any employment-related expenses paid by the taxpayer to an individual who bears to the taxpayer any relationship described in section 152(a)(1) through (8). These relationships are those of a son or daughter or descendant thereof; a stepson or stepdaughter; a brother, a sister, stepbrother, or stepsister; a father or mother or an ancestor, of either; a stepfather or stepmother; a nephew or niece; an uncle or aunt; or a son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, or sister-in-law. In addition, no credit is allowed with respect to the amount of any employment-related expenses paid by the taxpayer to an individual who qualifies as a dependent of the taxpayer for the taxable year within the meaning of section 152(a)(9), which relates to an individual (other than the taxpayer's spouse) whose principal place of abode for the taxable year is the home of the taxpayer and who is a member of the taxpayer's household.

(3) *Exception for payments to certain related individuals.* For taxable years beginning before January 1, 1979, a credit is allowed for the amount of any employment-related expenses paid by the taxpayer to an individual provided that neither the taxpayer nor his or her spouse is entitled to a deduction under section 151(e) (relating to deduction for personal exemptions for dependents) with respect to such individual for the taxable year in which the service is performed; and the service with respect to which the amount is paid constitutes employment within the meaning of section 3121(b). The following services performed for a taxpayer by a relative who is an employee of the taxpayer may qualify as employment within the meaning of section 3121(b):

(i) Services performed by the taxpayer's child age 21 or over.

(ii) Domestic services in the taxpayer's home performed by the taxpayer's parent if—

(A) The taxpayer has living in his or her home a child (as defined in section 151(e)(3)) who is under age 18 or who has a physical or mental condition requiring the personal care of an adult during at least 4 continuous weeks in the calendar quarter, and

(B) The taxpayer is a widow or widower or is divorced, or has a spouse living in the home who, because of a physical or mental condition, is incapable of caring for his or her child during at least 4 continuous weeks in the calendar quarter in which services are rendered.

(iii) Services of all relatives other than a child, spouse, or parent of the taxpayer.

For taxable years beginning before January 1, 1979, a credit is not allowed under section 44A with respect to employment-related expenses paid by the taxpayer to a relative for services which do not constitute employment under section 3121(b). Services performed by a relative do not constitute employment if they relate to the relative's trade or business the income from which is includible in computing the relative's net earnings for purposes of the self-employment tax under section 1401.

(4) *Payments to entities or partnerships.* If the services are performed by an entity or partnership, paragraph (a) (1) and (2) of this section is normally not applicable. If, however, the entity or partnership is established or maintained primarily to avoid the application of paragraph (a) (1) or (2) in order to permit the taxpayer to obtain the credit with respect to employment-related expenses, for purposes of this paragraph (a), the payments of employment-related expenses shall be treated as made directly to each owner of the entity or partner in proportion to his

or her share of the entity or partnership. A factor to consider for purposes of determining whether an entity or partnership is so established or maintained is whether the entity or partnership is set up solely to care for the taxpayer's qualifying individual and to provide household services to the taxpayer.

(5) *Illustrations.* The application of this paragraph may be illustrated by the following examples:

Example 1. For A's taxable year ending December 31, 1978, A, a divorced taxpayer, pays $5,000 of employment-related expenses to his mother for the care of his child age 5. A's mother cares for the child in her home. The services performed by A's mother do not constitute employment under section 3121(b). Accordingly, A is not allowed a credit with respect to the amounts paid to the mother for the care of his child.

Example 2. Assume the same facts as in *Example 1* except that A's taxable year under consideration begins after December 31, 1978. A is not entitled to a deduction under section 151(e) for his mother. Accordingly, A is allowed a credit with respect to the amounts paid to the mother for the care of his child even though the services performed by A's mother do not constitute employment under section 3121(b).

Example 3. For B's taxable year ending December 31, 1978, B, a divorced taxpayer, pays $6,000 of employment-related expenses to his sister (who is not a dependent of the taxpayer) for the care of his child. The services performed by B's sister in the care of his child constitute a trade or business the income from which is includible in computing net earnings for purposes of the self-employment tax under section 1401. Accordingly, B is not allowed a credit with respect to the amounts paid to the sister for the care of his child.

Example 4. Assume the same facts as in *Example 3* except that B's taxable year under consideration begins after December 31, 1978. B is allowed a credit with respect to the amounts paid to the sister for the care of his child, even though the services performed by B's sister do not constitute employment under section 3121(b).

(b) *Expenses qualifying as medical expenses.* An expense which may constitute an amount otherwise deductible under section 213, relating to medical, etc., expenses, may also constitute an expense with respect to which a credit is allowable under section 44A. In such a case, that part of the amount with respect to which a credit is allowed under section 44A will not be considered as an expense for purposes of determining the amount deductible under section 213. On the other hand, where an amount is treated as a medical expense under section 213 for purposes of determining the amount deductible under that section, it may not be treated as an employment-related expense for purposes of section 44A. The application of this paragraph may be illustrated by the following examples:

Example 1. In 1982, a calendar year taxpayer incurs and pays $5,000 of employment-related expenses during the taxable year for the care of his child when the child is physically incapable of self-care. These expenses are incurred for services performed in the taxpayer's household and are of a nature which qualify as medical expenses under section 213. The taxpayer's adjusted gross income for the taxable year is $100,000. Of the total expenses, the taxpayer may take $2,400 into account under section 44A; the balance of the expenses, or $2,600, may be treated as medical expenses to which section 213 applies. However, this amount does not exceed 3 percent of the taxpayer's adjusted gross income for the taxable year and is thus not allowable as a deduction under section 213.

Example 2. Assume the same facts as in *Example 1.* It is not proper for the taxpayer first to determine his deductible medical expenses of $2,000 ($5,000—[$100,000×3 percent]) under section 213 and then claim the $3,000 balance as employment-related expenses for purposes of section 44A. This is because the $3,000 balance has been treated as a medical expense in computing the amount deductible under section 213.

Example 3. In 1982, a calendar year taxpayer incurs and pays $12,000 of employment-related expenses during the taxable year for the care of his child. These expenses are incurred for services performed in the taxpayer's household, and they also qualify as medical expenses under section 213. The taxpayer's adjusted gross income for the taxable year is $18,000. The taxpayer takes $2,400 of such expenses into account under section 44A. The balance, or $9,600, he treats as medical expenses for purposes of section 213. The allowable deduction under section 213 for the expenses is limited to the excess of the balance of $9,600 over $540 (3 percent of the taxpayer's adjusted gross income of $18,000), or $9,060.

(Secs. 44A(g) and 7805 of the Internal Revenue Code of 1954 (90 Stat. 1565, 26 U.S.C. 44A(g); 68A Stat. 917, 26 U.S.C. 7805))

[T.D. 7643, 44 FR 50335, Aug. 28, 1979, as amended by T.D. 7951, 49 FR 18092, Apr. 27, 1984]